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CENTRAL INTELLIGENCE AGENCY
WASHINGTON, D.C. 20505

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15 February 1974

MEMORANDUM FOR: Mr. James Reddington
INR/REC
Room 8646
Department of State

SUBJECT : Bilateral Oil Proposals

In response to your request of 13 February 1974,
attached is a list of bilateral oil proposals and a
short article which provides comment on them. They
are unclassified,

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MAURICE C. ERNST
Director
Economic Research

Attachments

As stated

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Recent Bilateral Oil Proposals

Consumer	Producer	Details
Japan	Iran	Agreement in principle to provide a \$1 billion loan for a 500,000 b/d refinery in Iran in return for bulk of output. Refinery project, however, may hinge on outcome of negotiations for a petrochemical plant including an additional \$1 billion in credits.
	Iraq	Agreement initialled providing \$1 billion loan for an Iraqi refinery, LPG plant, petrochemical plant, and other industrial projects in return for 180,000-200,000 b/d of crude and products for 10 years, natural gas, and other projects.
	Saudi Arabia	Economic cooperation agreement to be signed in mid-February. In return, Japan hopes to line up long-term oil supply.
	Algeria	Japan negotiating credits for industrial projects in return for direct deal crude and LNG.
	Kuwait	Kuwait says it is ready to negotiate sale of oil as soon as a new participation agreement with Gulf/BP is signed.
West Germany	Iran	The West German government, negotiating on behalf of a German oil consortium, has agreed in principle to construct a 500,000 b/d refinery in Iran, reportedly at a cost of \$1.2 billion, in return for the output. The project may hinge, however, on outcome of negotiations for a \$1 billion petrochemical complex.

Recent Bilateral Oil Proposals
(continued)

Consumer	Producer	Details
	Abu Dhabi	The French, wishing to buy participation crude, have offered to build petro-chemical plant in return.
	Kuwait	France offered arms and large industrial investment in exchange for long-term oil deliveries. The size of the deal is subject to future negotiations and Kuwait approval in principle.
	Iran	Agreement in principle signed for \$5 billion in industrial projects. In return, France to get natural gas and oil exploration rights.

BILATERAL OIL PROPOSALS

The French Case

The French have been moving aggressively in the last three months to negotiate bilateral agreements with the major oil producers. They, like other big consumers, want to ensure access to the large oil supplies that someday will be controlled by the producer governments, and they see bilateral agreements as a good means of paying for the oil. Paris, of course, also wants a leg up on other consumers including fellow EC governments, and it has at least agreements in principle, if not confirmed deals, with several Middle East producers. The French took particular delight in announcing their multibillion dollar agreement with Iran on the eve of the Washington Energy Conference.

In the short run, the gain, if any, from such bilateral arrangements is largely political. Benefits in oil and potential foreign exchange earnings from the sale of industrial and military equipment are far in the future and uncertain at best.

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The agreement, which will entail considerable additional negotiation, involves about \$3 billion worth of energy-related projects already under discussion and a reported \$2 billion in new proposals. It calls for France to build several nuclear powerplants, a petrochemical complex, a steel plant, and several other industrial projects. It also calls for joint construction of a gas liquefaction plant and a fleet of LNG tankers.

Even if negotiations are successfully concluded, Paris may run into problems because the nuclear reactors to be provided to Iran probably will have to make use of licensed technology from the United States. All new reactors being built in France are either pressurized water reactors manufactured under license to Westinghouse or boiling water reactors under license to General Electric. If these systems are used in Iran, the French would either need to use US technology or encounter a long delay while they develop a technology of their own. France does have an advanced technology in fast breeder reactors, but this has not yet been developed to commercial status.

The status of recent French deals with other Middle East governments also is somewhat uncertain. There apparently have been no new developments in discussions with Kuwait concerning a swap of arms and industrial goods for crude oil. An agreement reportedly was concluded with Abu Dhabi to supply planes for oil, but the situation remains confused

regarding Paris' offer to build a petrochemical plant in return for oil. The agreement with Saudi Arabia is the most firm, and France is scheduled to take delivery of oil starting this year in return for constructing an oil refinery.

On balance, the French are no better off with regard to assured oil supplies than the other major consumers. They have much more negotiating to do and face problems in fulfilling some of the agreements. The producers have made few actual commitments of oil, and these are relatively small. Even potential foreign exchange earnings from earnings from deals with the producer governments will be stretched out over many years.

Flagging Producer Interest in Bilateral Deals

Some oil producers and consumers apparently are beginning to have second thoughts about the value of bilateral deals. Saudi Arabia and the United Kingdom, for example, have decided to shelve plans for an oil-for-goods agreement. Although Iran continues actively to pursue such deals, the Shah's motivation undoubtedly centers on deriving political advantage in his efforts to wrest OPEC leadership from the Saudis.

Aside from possible political advantages, there are no compelling reasons for the oil producers to make long-term bilateral deals for investment goods. They face no shortage of straight offers to supply these items. The producers do, however, have increasing reason to seek government-to-government deals of oil for cash. With their share of participation crude increasing, they are interested in increasing their sales to governments at high prices, minimizing the amount they sell back to the oil companies under the buy-back provisions of participation agreements.

Now that oil supply problems have eased, some consumers are beginning to see that the bilateral arrangements being negotiated will yield them very little. While the consumers have offered billions in loans, industrial equipment, and technical assistance, the producers frequently have made only vague promises of oil in return. For example, Japan has been negotiating an economic cooperation agreement with Saudi Arabia, but the Saudis have only hinted at making a separate oil purchase agreement with Tokyo. Even when specific commitments of oil have been made or are being discussed, the amounts are quite small relative to world oil trade, and in many cases deliveries will not start for several years. The total amount of crude oil and products involved in the major bilateral proposals now being negotiated could eventually result in deliveries of roughly 2 million b/d, equal to only about 7% of estimated January 1974 exports by OPEC members.

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